Supreme Court, U.S.
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No.

IN THE

Supreme Court of the United States

PETER S. VISINC, MICHAEL GRYNBERG, LEROY HIBBITTS, SAJID KALEEM AND PHILIP WEISBURGH, IRA,

Petitioners,

NORTEL NETWORKS CORPORATION, JOHN ANDREW ROTH, WILLIAM F. CONNOR, CHAHRAM BOLOURI AND FRANK DUNN

Respondents.

On Petition for Writ of Certiorari
To The United States Court of Appeals
For The Second Circuit

PETITION FOR WRIT OF CERTIORARI

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QUESTION PRESENTED

Even though: a) Plaintiffs purchased the very security at issue in the claims; b) during the defined class period; c) at prices which were indisputably inflated by Defendants' allegedly false and misleading statements; and d) the stock purchased by Plaintiffs dramatically declined in price when Defendants revealed the truth at the end of the class period, the Court of Appeals for the Second Circuit (the "Second Circuit") held that Plaintiffs lacked standing under Section 10(b) of the Securities Exchange Act of 1934 (the "Securities Exchange Act"), 15 U.S.C. § 78j, and Rule 10b-5 promulgated thereunder, 17 C.F.R. § 240.10b-5, because "[s]tockholders do not have standing to sue . . . when the company whose stock they purchased is negatively impacted by the material misstatement of another company, whose stock they do not purchase." The question therefore presented by this petition is:

> whether a purchaser of a security alleged to have been artificially inflated by Defendant's statements lacks standing under Section 10(b) of the Securities Exchange Act and Rule 10b-5 promulgated thereunder because the Defendant is not the issuer of the security which was purchased.

LIST OF PARTIES

The Plaintiffs ("Plaintiffs" or "Petitioners") are purchasers of the common stock of JDS Uniphase Corporation ("JDSU") during the period January 18, 2001 through February 15, 2001 (the "Class Period").[1] ¶ 31 (A-18) The Defendants are Nortel Networks Corporation ("Nortel" or the "Company"); John Andrew Roth, Nortel's Chief Executive Officer, President, and a Director of the Company at all material times; Frank Dunn, the Company's Chief Financial Officer throughout the Class Period; and Clarence J. Chandran, Nortel's Chief Operating Officer at all material times. ¶¶ 3, 32-35 (A-11, 18).[2]

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[1] Citations in this format are to the paragraphs of the Complaint, and, unless otherwise noted, to the Appendix below.

[2] On October 16, 2001, the district court consolidated, for the purposes of discovery, the instant case with a companion case brought against the Defendants by purchasers of Nortel securities. The district court denied Defendants' motion to dismiss the Nortel stock purchaser class action, finding that the plaintiffs had adequately alleged Defendants' scienter and that Defendants' statements, including those at issue in the instant case, were actionable. *In re Nortel Networks Corp. Sec. Litig.*, 238 F. Supp. 2d 613 (S.D.N.Y. 2003). The caption below also references the following plaintiffs in the Nortel class action, though they are not parties to this Petition: Ontario Public Service Employees Union Pension Trust Fund; Eli Weinstein, M&G Investment Management Ltd., and AXA Investment Managers, U.K., Ltd., on behalf of all others similarly situated.

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OPINION BELOW

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STATEMENT OF JURISDICTION

The Court has jurisdiction under 28 U.S.C. § 1254(1). The Opinion was entered on May 19, 2004. Rehearing, timely requested, was denied on July 14, 2004.

APPLICABLE STATUTORY AND REGULATORY PROVISIONS

The text of Section 10(b) of the Securities Exchange Act, 15 U.S.C. § 78j, and Rule 10b-5 promulgated thereunder, 17 C.F.R. § 240.10b-5, are reprinted at App. 50a and App. 52a, respectively. The text of Section 3(a)(10) of the Securities Exchange Act, 15 U.S.C. § 78c(a)(10) is reprinted at App. 49a. The text of Section 18 of the Securities Exchange Act, 15 U.S.C. § 78r, is reprinted at App. 51a.

STATEMENT OF THE CASE

Petitioners are purchasers of the common stock of JDSU during the Class Period. Plaintiffs allege that Defendants engaged in a fraudulent scheme designed to allow Nortel: (a) to acquire JDSU's "pump laser" business (the "Laser Business") with inflated Nortel stock; and (b)

to complete a $1.5 billion offering of Nortel debt securities. ¶¶ 4-5, 187-207 (A-11, 62-67).

Nortel's false and misleading statements not only inflated Nortel's stock, but also JDSU's. By the start of the Class Period, the market was aware that Nortel and JDSU had reached an agreement in principal for the sale of the Laser Business and Nortel would likely transfer *$2.5* to *$3.0 billion* of its stock to JDSU in exchange for that business. ¶¶ 7, 12, 54, 121-23 (A-12-13, 24, 41-42). Given the efficient market for JDSU's stock, JDSU investors factored this potential asset, which equaled 10% to 12% of JDSU's total assets at that time, into their assessment of JDSU's stock price.[3] Moreover, JDSU investors were aware that Nortel was also JDSU's largest customer, supplying 10%-15% of JDSU's total revenues, and that Nortel's statements regarding the status of its end-user fiber optic business provided critical information for assessing the demand for JDSU's fiber optic components. ¶¶ 6, 12, 123 (A-11, 13, 41-42). The quest for such information was, at that point in time, keen, given market rumors of a potential slowdown in the fiber optic field. ¶ 56 (A-25).

As a result, throughout the Class Period, Defendants' positive statements concerning Nortel's operations and prospects had a direct inflationary impact upon the market price of JDSU stock. When Nortel announced, on the first day of the Class Period, continued strong demand for its products and that it would report earnings and revenue growth of 30% for the year, JDSU's stock price rose $6.56 per share, a rise attributed by market pundits to Nortel's disclosures. *See* ¶¶ 12, 128 (A-13, 43).

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[3] In its Form 10-Q for the quarter ended December 30, 2000, JDSU reported assets of $24.945 billion. Thus, the $2.5 billion in Nortel stock received by JDSU in February 2001 equaled 10% of JDSU's reported assets, and the $3.0 billion in total consideration to be received by JDSU in connection with the transaction equaled 12% of those assets. Relying upon *Kramer v. Time Warner, Inc.*, 937 F.2d 767, 774 (2d Cir. 1991), Petitioners asked the Second Circuit to take judicial notice of the Form 10-Q in resolving their appeal.

On February 6, 2001, when Defendants announced the final terms of the Laser Business transaction and that Nortel would pay JDSU $2.5 billion in Nortel stock and would either make significant future purchases of JDSU products or pay JDSU as much as $500 million more in Nortel stock, JDSU's stock price rose $1.81 per share. ¶¶ 15, 134-38 (A-14, 44-46), ¶¶ 17, 139 (A-14, 46).[4]

On February 12, 2001, when Nortel and JDSU announced the closing of the Laser Business transaction, ¶¶ 19-20, 94 (A-15, 33), which was subject to the "customary closing conditions", one of which was the selling company's attestation that it was unaware of any material change to its operations or financial prospects. ¶¶ 15, 19, 135, 137, 140 (A-14, 15, 44-45, 46). The consummation of this transaction further confirmed to JDSU investors the potential appreciation of what was then one of JDSU's principal assets, $2.5 billion in Nortel stock and a commitment for a material amount of increased future purchases of JDSU's products. ¶¶ 136, 143-44 (A-45, 47).

Having achieved the objective of their fraud, Defendants revealed, just *three days* after the Laser Business transaction closed, that: (a) in contrast to their prior guidance of a profit of 16 cents per share in the first quarter, Nortel would lose 4 cents per share; (b) Nortel's revenues for the quarter would be $1.7 *billion* less than projected at the beginning of the Class Period, just four weeks earlier; (c) Nortel's revenue growth for the year would be 15%, not the 30% previously announced; (d) Nortel's earnings growth for 2001 would be 10% rather than 30%; and (3) Nortel would be cutting 10,000 jobs. ¶¶ 22-23, 157 (A-16, 51).

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[4] Defendants and analysts noted that these revenue commitments represented an increase in Nortel's purchases from JDSU, ¶¶ 16, 144-45, 150 (A-14, 47, 49), and would enhance JDSU's ability to meet its existing projections for fiscal 2001. ¶¶ 16, 144-45 (A-14, 47).

The stunning revelations that the $2.5-$3.0 billion in Nortel stock received by JDSU was worth far less than that amount and that Defendants had vastly overstated Nortel's prospects, prompted a $9.31 per share decline in the market price of JDSU stock to $35.81, a one-day decline of 21%, ¶¶ 24, 163 (A-16, 55), on volume of 99 million shares, making it the most actively traded NASDAQ stock. ¶¶ 24 (A-16).

Numerous analysts immediately lowered their ratings on JDSU stock and specifically noted that their revised guidance and the decline in JDSU's stock price were directly caused by Nortel's revelations. ¶¶ 164-68 (A-55-56). Various analysts questioned the credibility of Defendants' prior statements and flatly rejected Defendants' contention that they had just learned of the slow down in Nortel's business. ¶¶ 161(a)-(e) (A-52-54). Likewise, JDSU indicated that it was "shocked" by Nortel's belated announcements, ¶¶ 170-72 (A-56-57), and informed investors that it understood why analysts cut their JDSU forecasts in response to Nortel's disclosures. ¶ 169 (A-56). While JDSU indicated that it would consider filing suit against Nortel as a result of the Laser Business transaction, it further indicated that it would probably not be able to do so, given the business relationship between the two companies. ¶ 170 (A-56-57).

Plaintiffs' Amended Complaint, filed on January 4, 2002, alleged claims under Section 10(b) of the Exchange Act and Rule 10b-5 on behalf of JDSU purchasers during the Class Period. Though Defendants' statements were clearly material to JDSU investors, a fact which, given the reaction of JDSU's stock price to such statements, has never been contested by Defendants, the district court found that Plaintiffs did not satisfy the "purchaser/seller" requirement for Section 10(b) claims set out in *Blue Chip Stamps v. Manor Drug Store*, 421 U.S. 723 (1975) because Defendants' statements did not relate to JDSU. App. 26a-28a. Additionally, the district court held that Defendants' statements were not issued "in connection with" Plaintiffs'

purchases since they did not go to the "value" of the stock purchased by Plaintiffs.[5] App. 28a-31a.

The Second Circuit declined to discuss the issue of whether Defendants' conduct or statements were "in connection with" Plaintiffs' purchases and, instead, held that Plaintiffs lacked standing because the company issuing the material statements which artificially inflated the securities purchased by Plaintiffs was not the issuer of the securities purchased by Plaintiffs. To reach this conclusion, the Second Circuit ignored the holding of *Blue Chip*, that a plaintiff has standing if he purchases or sells securities, choosing instead to rely on *Blue Chip's dicta* wherein this Court explained the application of the general rule to the facts of that case. No court since *Blue Chip* was decided almost thirty years ago has ever interpreted this *dicta* as limiting Plaintiff's standing to only those who purchased the securities of the Defendant which issues the alleged false or misleading statements. The Opinion improperly shifts the focus of standing from a plaintiff's conduct (the act of purchasing or selling the security at issue) to the type of defendant issuing the misrepresentations. Whether defendant is a proper defendant is a question falling under the purview of the "in connection with" component of Section 10(b).

Moreover, it is clear that, in this instance, Defendants' statements "relate[d]" to JDSU, since the price of that security fluctuated dramatically in response to Defendants' public statements. In fact, on various occasions, Defendants specifically mentioned JDSU in their false and misleading statements. ¶¶ 136-138 (A-45-46) (press release describing the transfer of $2.5 billion in Nortel stock to JDSU and the increased purchasing requirements "intended to enhance the business relationship between both parties.") Even if *Blue Chip* established the standing requirement that Defendants'

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[5] Prior to the district court's opinion, Plaintiffs brought to the district court's attention *S.E.C. v. Zandford*, 535 U.S. 813 (2002), which noted that neither the SEC nor this Court has ever required that a statement go to the value of a security in order for a defendant's conduct to be "in connection with" a purchase or sale. *Id.* at 820.

statements must relate to the security purchased, which it does not, it is clear that *Blue Chip* confirms, rather than negates, Plaintiffs' standing.

To reach its conclusion, the Second Circuit was forced to rewrite Section 10(b) and Rule 10b-5, which make clear that the statute applies whenever a plaintiff purchases or sells "any security." Disregarding this Court's directive that unambiguous statutory language is to be followed ("any" means any), the Second Circuit, relying solely on a law review article which, upon inspection, does not support its conclusion, interpreted the phrase to mean any *type* of security of the company issuing the statement, that is bond, common stock, etc. The Court's conclusion is particularly untenable given that the Securities Exchange Act defines a "security" to include any type of security, rendering the Second Circuit's interpretation of "any" redundant. The Second Circuit's conclusion also contravenes this Court's pronouncements that the repeated use of the term "any" in Section 10(b) and Rule 10b-5 demonstrates the intention of Congress and the Securities Exchange Commission ("SEC") to broadly proscribe all conduct that could mislead investors.

The Second Circuit further disregarded this Court's exhortations that Section 10(b) is to be applied flexibly so as to promote full disclosure and its application is not limited to garden-variety frauds. In addition, the Opinion undermines an extensive body of Supreme Court and circuit court law directing that the "in connection with" phrase of Section 10(b) is satisfied whenever a defendant's conduct or statements "touch" a plaintiff's purchase or sale. Left unaltered, the Opinion mandates that in the Second Circuit, in any number of instances, defendants' conduct may be in connection with plaintiffs' purchases or sales, yet plaintiff will lack standing to ever reach the issue.

The Second Circuit noted its concern that finding Plaintiffs had standing would open a floodgate of litigation as investors in one company routinely sued

other companies for statements they issue about their companies or industries. Initially, this hypothetical concern finds no basis in history, as Plaintiffs found just *several* cases wherein there was such a close nexus between statements by a defendant which was not the issuer of the security purchased and plaintiffs' purchases of such securities that the "in connection with" component of Section 10(b) was satisfied. Defendants found *no cases* wherein any court had either denied standing or found defendants' statements not to be "in connection with" plaintiffs' purchases because plaintiffs purchased securities which were not those of the company issuing the challenged statements. Here, that nexus is supplied by a pending, and then finalized, transaction wherein JDSU would, and did, acquire 65.7 million shares of Nortel stock, equaling 10-12% of JDSU's total assets. While there is no doubt, here, that Defendants' statements were material to JDSU investors and, thus, "in connection with" their purchases, in the normal course, statements by one company will not be material to investors in the stock of another company. The analysis of the nexus between defendants' statements or conduct and plaintiffs' purchases is one that involves the "in connection with" component of Section 10(b), not whether the plaintiffs have standing to even present their case that defendants' statements artificially inflated the securities they purchased.

The Second Circuit incorrectly compared the Plaintiffs to those in *Blue Chip*. None of the vagarities of proof present in *Blue Chip* are present here, however, since all Plaintiffs purchased the stock at issue in their claims, JDSU. The Second Circuit's sole support for its conclusion, that Plaintiffs would have to orally prove that they relied on the Defendants' statements, ignores the very essence of an efficient market. All material information, not just statements uttered by the issuer of a security, is digested by such a market and reflected in the stock's price.

REASONS FOR ALLOWANCE OF THE WRIT

I. The Second Circuit Has Decided An Important And Recurring Issue - Standing - In a Manner That Creates An Intolerable Conflict With This Court's Prior Opinions And In A Manner Which Will Undermine The Integrity of the Market.

The Second Circuit's Opinion represents one of the most constrictive interpretations ever of the federal securities laws. In the Second Circuit, at least the following types of defendants who have previously come within the purview of the statute and Rule 10b-5 now enjoy immunity from liability: a) brokers who lie to their customers about the securities their clients purchase, since the plaintiffs did not purchase the stock of the brokerage firm; b) accountants issuing false opinions about the financial statements of publicly-traded companies, since plaintiffs did not purchase stock in the accounting firm; c) underwriters who lie about companies they take public since plaintiffs did not purchase the underwriter's stock; and d) since there has never been multiple standards of standing under Section 10(b) for misrepresentation and fraudulent act cases (which was also a basis of (Plaintiffs' claims), any of the other knowing participants in frauds, such as banks. The Second Circuit's Opinion has the potential, literally, to unravel the markets' continuing effort to regain investor confidence.

Interpreting *Blue Chip's dicta* relied on by the Second Circuit as limiting standing to those buying the securities of the company issuing the challenged statements reads out of existence *Blue Chip's* repeated pronouncements that it is the mere act of purchasing or selling securities that confers standing. *No court, since Blue Chip was decided almost 30 years ago, has read the opinion to mean what the Second Circuit read into it. Blue Chip* confirms, not negates, the Plaintiffs' standing.

The factual scenarios under which the Opinion denies investors relief or, alternatively, immunizes wrongdoing is extensive. In addition to those examples set forth above, companies will be encouraged to falsely denigrate their competitors' products, knowing that sellers of the competitors' stock have no standing to sue them, nor would such sellers be able to sue the issuer of the securities sold, since it issued no misrepresentations. Similarly, in a joint-venture between Company A, privately held, and Company B, publicly traded, involving product (or drug) development or testing, Company A could publicly lie at will (even with the secret encouragement of Company B) about the status of such products. Though such statements would likely have a direct inflationary impact on the market price of Company B's securities, purchasers of those securities would be unable to sue either party since they did not purchase Company A's securities and Company B issued no statements. Further, as this case makes clear, Company A, in the process of selling material components or divisions of its business to Company B, can openly overstate the financial condition of such components or divisions without fear of reprisal from purchasers of the securities of Company B, whose securities may well have reflected the false valuation of the acquired component or division.

In *Blue Chip,* this Court held repeatedly only that a plaintiff must purchase or sell securities to have standing under Section 10(b), not that plaintiff must purchase or sell the security of the company issuing the false statement. *See* 421 U.S. at 730 (*Birnbaum* "concluded that the plaintiff class for purposes of a private damage action under Section10(b) and Rule 10b-5 was limited to *actual purchasers or sellers*") (emphasis added); *Id.* at 731-32 (*Birnbaum* "conclu[ded] that the plaintiff class for purposes of Section10(b) and Rule 10b-5 private damage actions is limited to purchasers and sellers of *securities*") (emphasis added); *Id.* at 734 ("When Congress wished to provide a remedy to those *who neither purchase nor sell securities*, it had little trouble in doing so expressly.") (emphasis added); *Id.* at 734 ("[A] putative plaintiff, *who neither purchases nor sells securities* but

sues instead for intangible economic injury such as loss of a non-contractual opportunity to buy or sell, is more likely to be seeking a largely conjectural and speculative recovery in which the numbers of shares involved will depend on the plaintiffs' subjective hypothesis.") (emphasis added); and *Id.* at 735 (the justification for permitting a party deceived by a contract made in violation of the Exchange Act to void such an agreement "is absent when there is no actual *purchase or sale of securities*") (emphasis added).

Blue Chip explained that three classes of potential litigants are prevented by the purchaser/seller requirement from alleging Section 10(b) claims: those who say they would have purchased had they known the truth; those who say they would have sold had they known the truth; and those whose holdings are diminished in value due to some corporate or insider activities. *Id.* at 737-38. Here, Plaintiffs fit none of these categories, nor did the Second Circuit find that they did.[6]

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[6] While the district court held that Plaintiffs allege derivative claims, it is clear they do not. The crux of Plaintiffs' claims is that they were directly injured when they purchased JDSU stock at prices artificially inflated by Defendants' false pronouncements. Those claims are direct and belong solely to the class alleged in Plaintiffs' Complaint. *See, e.g., Kusner v. First Pennsylvania Corp.*, 531 F.2d 1234, 1239 (3rd Cir. 1976) ("If the purchasers can prove they parted with that consideration as a result of material misrepresentations in a prospectus, they may recover a direct action whether or not their interest in the corporation would support a derivative suit."); *Muzinich Co., Inc. v. Raytheon Co.*, No. CV-01-284-5-BLW, slip op. 4 (D. Idaho May 1, 2002) ("The plaintiffs [were] . . . induced to purchase stock by fraud. Raytheon knew that its false statements might be relied upon by investors, and plaintiffs did so. Thus, plaintiffs are suing for their own injury caused by Raytheon's statements.") (A-656); *Powers v. Ostreicher*, 824 F. Supp. 372, 378 (S.D.N.Y. 1993) (direct suit allowed where defendant made a misrepresentation that induced a shareholder to pay an inflated price for his stock). Plaintiffs' claims do *not* involve any indirect injury they may have suffered due to JDSU's acquisition of Nortel stock at inflated prices.

The injury alleged by plaintiffs is one that JDSU did not suffer because it did not purchase its own stock. ¶¶ 12, 17, 26, 55, 221,

Blue Chip did not seek to define what types of particular misrepresentations support a § 10(b) claim or, as the Second Circuit interpreted the opinion, who must issue a misrepresentation before a plaintiff has standing. Such matters present issues properly analyzed as questions of materiality or under the "in connection with" requirement, elements of a Section 10(b) claim not addressed in *Blue Chip*. *See, e.g., Semerenko v. Cendant Corp.*, 223 F.3d 165, 176 (3d. Cir. 2000); *In re Ames Dept. Stores Inc. Stock Litig.*, 991 F.2d 953, 967 (2d Cir. 1993).[7]

Standing defines the universe of people who have suffered the type of injury that allows them to pursue a particular claim. *See, e.g., Blue Chip*, 421 U.S. at 733 ("The longstanding acceptance by the courts, coupled with Congress' failure to reject *Birnbaum*'s reasonable interpretation of the wording of § 10(b), wording which is directed toward injury suffered 'in connection with the purchase or sale' of securities, argues significantly in favor of acceptance of the *Birnbaum* rule by this Court.") When *Blue Chip* noted that investors had standing if they purchased or sold the stock "in question" or "at issue," it was describing the universe of plaintiffs who could allege a Section 10(b) claim, not the type of misconduct that would support such a cause of action. Thus, when this Court concluded that only those investors who allege that they suffered damages as a result of a purchase or sale of the securities "at issue" or "in question" have standing, it was referring to the purchase or sale of the securities at issue or in question in plaintiffs' *claims*, and not to the subject matter of defendants' statements. Here, there is no doubt that it is JDSU stock that is "in question" or "at

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227, 228 (A-5, 6, 17, 24-25, 71, 73). Pursuant to *Blue Chip*, JDSU has no standing to bring the claims asserted by the instant Plaintiffs.

[7] While *Blue Chip* referenced Section 10(b)'s "in connection with" language as support for the proposition that the SEC intended for an investor to make a purchase or sale before liability would attach for a Rule 10b-5 violation, *Blue Chip* does not purport to determine the scope of the "in connection with" requirement. *Blue Chip*, 421 U.S. at 733.

issue" in Plaintiffs' claims because Plaintiffs seek to recover the money they overpaid for such shares due to Defendants' misrepresentations. ¶ 31 (A-18).

This conclusion is bolstered by the text of § 18 of the Securites Exchange Act, 15 U.S.C. § 78r, a statute *Blue Chip* relied upon as support for adopting the purchaser/seller requirement. *See Blue Chip*, 421 U.S. at 735. Section 18 provides that persons who make false statements in documents filed with the SEC are "liable to *any* person . . . who, in reliance upon such statement, shall have purchased or sold *a security at a price which was affected by such statement* . . ." App. 51a, 15 U.S.C. § 78r (emphasis added); *see also Blue Chip*, 421 U.S. at 736. Thus, like Rule 10b-5, the express terms of Section 18 do not limit the potential plaintiffs in a securities fraud action to purchasers of the securities of the issuer who made false representations. As this Court recognized in *Blue Chip*, it would be anomalous to have the scope of liability imposed by express causes of action created by the Securities Exchange Act, such as Section 18, be different than the liability imposed by implied causes of action, such as those for violation of Section 10(b). *See Blue Chip*, 421 U.S. at 736.

The language from *Blue Chip* cited by the Second Circuit is not its holding, but was expressly stated to be this Court's application of the general rule to the facts at hand in that case. Thus, after repeatedly announcing merely that those who refrain from buying or selling do not have standing, and that those who purchase the security "at issue" or "in question" have standing, this Court stated, in *dicta*, that "[t]he virtue of the *Birnbaum* rule [i.e., the purchase/seller requirement], simply stated, *in this situation*, is that it limits the class of plaintiffs to those who have least dealt in the security to which the prospectus, representation or omission relates." *Blue Chip*, 421 U.S. at 747 (emphasis added). Underlying this *dicta* was the fact that the plaintiff in *Blue Chip* alleged that he had read the defendants' prospectus and had it not improperly painted a negative picture of the

defendant corporation's prospects, he would have purchased defendant's stock.

Moreover, the context of this passage from *Blue Chip* cited by the Second Circuit confirms this Court's concern that mere market bystanders may assert unfounded claims:

> The virtue of the *Birnbaum* rule, simply stated, in this situation, is that it limits the class of plaintiffs to those who have at least dealt in the security to which the prospectus, representation, or omission relates. And their dealing in the security, whether by way of purchase or sale, will generally be an objectively demonstrable fact in an area of the law otherwise very much dependent upon oral testimony. In the absence of the *Birnbaum* doctrine, bystanders to the securities marketing process could await developments on the sidelines without risk, claiming that inaccuracies in disclosure caused nonselling in a failing market and that unduly pessimistic predictions by the issuer followed by a rising market caused them to allow retrospectively golden opportunities to pass.

Id. at 747. Clearly, this Court's focus was upon the verifiability of claims based upon actual purchases and sales, as opposed to speculative and perhaps completely concocted causes of action based upon purchases and sales from which investors supposedly refrained. *Id.* at 734-35.

Plaintiffs' purchases of JDSU stock are the exact type of concrete, ascertainable, events that this Court found eliminates the vagaries of proof addressed in *Blue Chip*. *Id.* at 742 ("The fact of purchase of stock and the fact that sale of stock are generally matters which are verifiable by documentation, and do not depend upon oral recollection, so that failure to qualify under the *Birnbaum*

rule is a matter that can normally be established by Defendant . . ."). The context of *Blue Chip's* use of the word "relates" confirms that the Second Circuit endowed that phrase with significance the term was never intended to possess.[8]

In *Basic*, this Court implicitly rejected the premise upon which the Opinion is grounded: that public statements issued by a company are directed only to specific targeted investors. Ironically, the Second Circuit, in holding that "it is not a bar to a 10b-5 action that the false and misleading statements in a Registration Statement are pertaining to an issue of a security, be it preferred stock, reset note, or debenture, or otherwise, which is not the security purchased", *Ames*, 991 F.2d at 964,[9] and in rejecting the argument that liability cannot attach where defendants' statements were supposedly addressed to "discrete groups of potential purchasers, not issued to the public generally," *Ames*, 991 F.2d at 965, explained:

> in *Basic, Inc.*, the defendants, in response to stock market movements, said there were no ongoing merger discussions or known corporate developments, and the plaintiffs, common stock holders, sold their stock after these denials; in fact, the company had been approached as to a merger, and indeed the merger took place after plaintiffs' sales. *The statements neither had any specific audience nor were related to any specific security, but were*

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[8] Since Defendants' statements were material to JDSU and actually discussed JDSU on occasion, it is also beyond cavil that Defendants' statements "relate[d]" to JDSU's stock.

[9] *Accord Itoba Ltd. v. LEP Group Pk.*, 54 F.3d 118, 123 (2d Cir. 1995) ("[A] Rule 10b-5 action is not barred because a false and misleading statement in an SEC filing pertains to a security that is not the security purchased.").

> *held, on the basis of a fact-specific inquiry, to be material and to permit the application of a rebuttable presumption of reliance, supported in part by the fraud-on the-market theory. Id. at 241-45, 108 S.Ct. at 988-90.* . .while *Basic, Inc.,* addressed the reliance and materiality requirements, rather than the connection requirement, *the fraud-on-the-market theory is premised on the notion that fraud can be committed by any means of disseminating false information into the market on which a reasonable investor would rely.* Because the fraud on the market may taint each purchase of *the affected stock,* each purchaser who is thereby defrauded is defrauded by reason of the publicly disseminated statement. *If such a straightforward cause and effect is not a connection, then the Rule would not punish a particularly effective means of reducing the integrity of, and public confidence in, the securities markets.* The "in connection with" language was chosen in an effort to broaden the reach of the Rule to achieve precisely these aims, *see, e.g., SEC v. Texas Gulf Sulphur,* 401 F.2d at 860-62; it should not be used to defeat them.

Ames, 991.F2d at 967-68 (emphasis added). Here, there is no doubt that the cause and effect test accepted by *Ames* is satisfied. Defendants' false and misleading statements regularly inflated JDSU's stock price.

The Second Circuit's conclusion that the supposed need for oral proof of reliance in this case renders the current situation comparable to that present in *Blue Chip* is contradicted by *Basic,* which held that an efficient market absorbs, and reflects in its price, *all* material information and that plaintiffs satisfy the reliance element of their claim merely by relying on the integrity

of the market price of the security purchased. *Basic*, 485 U.S. at 244-47. *See also In re Burlington Coat Factory Sec. Litig.*, 114 F.3d 1410, 1425 (3d Cir. 1977) (". . . efficient markets are those in which information important to reasonable investors . . . is immediately incorporated into stock prices."). Plaintiffs alleged that JDSU's stock traded in an efficient market, ¶¶ 176-77, (A-58-60), and even demonstrated the efficiency of that market by pleading the stock's movement whenever Defendants spoke and how analysts attributed those price movements to Defendants' statements. *See supra.* Plaintiffs need not, therefore, rely on oral proof to satisfy the reliance element of their Section 10(b) claim.

II. The Second Circuit's Interpretation Of Standing Cannot Be Squared With The Text Of Section 10(b) And Rule 10b-5.

Section 10(b) and Rule 10b-5 unambiguously confer standing on purchasers or sellers of "any security." In contravention of *Central Bank of Denver, N.A. v. First Interstate Bank of Denver, N.A.*, 511 U.S. 164, 173 (1994), which reaffirmed that, absent ambiguity, courts are obligated to follow the text of Section 10(b), the Second Circuit took an unprecedented reading of Section 10(b), concluding that "any security" actually means *any type* of security of the company issuing the challenged statements, such as a bond, common stock, etc. Had Congress and the SEC, however, intended such a limit on standing they were fully capable of accomplishing that objective. By rewriting this unambiguous phrase ("any" means any), the Second Circuit ignored the clear intent of Congress and this Court's admonition that "[t]hese proscriptions, by statute and rule, are broad and, by repeated use of the word 'any' are obviously meant to be inclusive." *Affiliated Ute Citizens v. United States*, 406 U.S. 128, 151 (1972).[10]

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[10] The Opinion's sole support for reading "any security" to mean any type of security of the company issuing the statement is a treatise, which merely states that "any security" encompasses all types of securities, even those exempt from registration. The word "any",

Moreover, the Second Circuit's interpretation of "any" is redundant of the definition of "security" included in the Securities Exchange Act. 15 U.S.C. § 78c(a)(10) defines security as "any note, stock, treasury stock, security, future, bond, debenture, . . . , investment, contract, . . . , or, in general, any interest or instrument commonly known as a 'security'." 15 U.S.C. § 78c(a)(10). App. 49a. Congress would not have used the term "any" to connote the same meaning as the word "security", which immediately follows it.

III. The Second Circuit's Limitation Of A Plaintiff's Standing Conflicts With Numerous Decisions Issued By This Court Interpreting The "In Connection With" Clause Of Section 10(b) And Directing That This Statute be Interpreted Flexibly, with a Goal of Promoting Full Disclosure.

The Opinion ignores extensive Supreme Court precedent directing that Section 10(b) is not to be interpreted ". . . technically and restrictively, but flexibly to effectuate its remedial purposes," and should be interpreted to implement a policy of full disclosure. *See Superintendent of Ins. v. Bankers Life & Cas. Co.*, 404 U.S. 6, 12 (1971); *Affiliated Ute*, 406 U.S. at 151; *Basic*, 485 U.S. at 230; *SEC v. Zandford,* 535 U.S. 813, 819-20, (2002). In the Second Circuit, numerous investors may now have no relief under the federal securities laws even if, as here, they have adequately alleged every element of their Section 10(b) claim.

The Opinion also undermines an extensive body of Supreme Court and circuit court precedent interpreting the "in connection with" component of Rule 10b-5. This Court has held that defendants' conduct or statements are "in connection with" a plaintiff's purchase any time they

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however, not only encompasses different types of securities *but also* any issuer's securities. The Opinion cites no authority for its conclusion that "any" must mean one or the other.

"touch" that purchase, *Bankers Life*, 404 U.S. at 12, and recently reaffirmed that it has repeatedly read "in connection with" "flexibly to effectuate its remedial purposes." *Zandford*, 535 U.S. at 819. *See also U.S. v. Russo,* 74 F.3d 1383, 1391 (2d Cir. 1996) (noting the "expansive approach" adopted by the Supreme Court in interpreting the "in connection with" requirement). The Second Circuit previously held that defendants' statements are "in connection with" plaintiffs' purchases, in an efficient market, whenever those statements are material to investors. *Ames*, 991 F.2d at 964. *Accord In re Carter Wallace, Inc. Sec Litig.*, 150 F.3d 153, 256 (2d Cir. 1998) (wherein "a claim is based on the fraud-on-the-market theory, a straightforward cause and effect test is applied.") (internal quotations and citation omitted). The Opinion permits defendants to accomplish indirectly (through the standing requirement) what this Court and the appellate courts have held they may not do directly (through the "in connection with" requirement). *See, e.g., Zandford*, 535 U.S. at 820; *Ames*, 991 F.2d at 967. That the courts apply a broad reading of "in connection with", and even that defendants' conduct is demonstrably "in connection with" plaintiffs' purchases, will be little comfort to whole categories of investors denied standing.

IV. The Second And Third Circuits Are In Conflict As To Whether A Plaintiff Who Purchased Securities Inflated By Statements Uttered By Other Than The Company Whose Securities Plaintiff Purchased Has Standing.

The Opinion is contrary to the Third Circuit's opinion in *Semerenko v. Cendant Corp.*, 223 F.3d 165 (3d Cir. 2000). Relying on the *Ames* materiality test, *Semerenko* held that the district court in that case improperly held that Cendant Corp.'s misrepresentations about Cendant made during a tender offer for *ABI* were not "in connection with" the plaintiffs' purchases of *ABI* stock. *Semerenko,* 233. F.3d at 169, 175-76. (Plaintiffs adequately plead a §10(b) claim even though "[t]he complaint does not allege that any member of the class purchased securities issued by Cendant, or that any

member of the class tendered shares of ABI common stock to Cendant.").

The Second Circuit's effort to distinguish *Semerenko* is legally untenable. The Second Circuit stated that it was not resolving whether a plaintiff's purchase of an acquiree's stock in a tender offer would have standing to sue the acquiror for false statements issued by the acquiror, because it would have to analyze the nexus or importance of the proposed transaction to plaintiff's purchase. This sliding scale of standing (how important the proposed transaction is to plaintiff's reason for buying) has never been accepted by any court and will open a Pandora's box of litigation on a case-by-case basis as to whether plaintiffs have standing based on the status of the defendant. The analysis suggested by the Opinion is, actually, exactly what the "in connection with" analysis is all about: were defendants' statements material to investors and therefore "in connection with" their purchases? Moreover, the Second Circuit accepted that Defendants' statements were material to JDSU purchasers, App. 13a, (wherein the court's holding acknowledges the materiality of the statements), and, thus, "in connection with" Plaintiffs' purchases. *See Ames*, 991 F.2d at 964. In fact, the nexus between Defendants' statements and Plaintiffs' purchases was greater than that of the defendants' statements and plaintiffs' purchases in *Semerenko* since, here, the material asset acquisition was completed while, in *Semerenko,* the merger never came to fruition.

Any factual differences between *Semerenko* and this case go only to whether Defendants' statements were material to such investors. Courts have consistently held that representations made by market participants during circumstances analogous to those presented here, such as uncompleted mergers or tender offers, may be material to investors. *See Basic*, 485 U.S. at 236 ("we therefore find no valid justification for artificially excluding from the definition of materiality information concerning merger discussions, which would otherwise be considered significant to the trading decision of a reasonable

investor, merely because agreement in principal as to price and structure has not yet been reached by the parties on their representations"); *Semerenko*, 223 F.3d at 177 ("It is well established that information concerning a tender offer or a proposed merger may be material to persons who trade in the securities of the target company, despite the highly contingent nature of both types of transactions"). Just as the financial condition of an offeror in a tender offer or merger "is likely material to investors considering purchase of the target company's stock," the financial condition of Nortel, which would determine the current and future value of the 65.7 million shares of Nortel stock that JDSU was to, and did, acquire by selling its Laser Business to Nortel, was material to JDSU investors.

The reason *Semerenko* did not discuss standing is because no court, prior to this case, read *Blue Chip* to mean standing only exists whenever plaintiffs purchase the security of the company issuing the false statements. Instead, it has been universally accepted that plaintiffs have standing whenever they purchase the security at issue in their claims. This fact demonstrates the error in the Second Circuit's conclusion that it is "unreasonable to assume that the [*Semerenko*] Court believed standing to be so clearly established that it did even warrant discussion in the opinion." App. 11a-12a. Respectfully, it is far more unreasonable to assume that the distinguished panel from the Third Circuit wholly missed this purportedly key issue. The Third Circuit analyzed the plaintiffs' claims in the exact same way every other Court has for the last thirty years: so long as plaintiffs purchased the security at issue in their claim, was defendants' conduct "in connection with" plaintiffs' purchases?

V. The Second Circuit's Policy Concerns Are Entirely Speculative.

Upon inspection, the Opinion's constrictive reading of Section 10(b) is premised exclusively on a policy concern that conferring standing in this case would open a

floodgate of litigation. This policy argument, however, has *no* factual support. Absent unique circumstances such as those present here, statements by one company will not be material to investors in another company's stock.

For example, statements by *Boeing* regarding the strength of its business will not typically be material to purchasers of the stock of a conglomerate such as General Electric ("GE"), even assuming plaintiffs are able to adequately allege the statements were false and satisfy all other requirements under the Private Securities Litigation Reform Act. Although Boeing may purchase jet engines from GE, Boeing's statements would pertain to just *one* of GE's customers for a *single* product of *one* of its many subsidiaries. As such, there would not likely be a market reaction to such statements.

Notwithstanding the fact that it has been sixty years since Congress adopted Section 10(b) and the SEC adopted Rule 10b-5, a) Defendants found *no* cases wherein any court had either denied standing or found defendants' statements not to be "in connection with" plaintiffs' purchases because plaintiffs purchased securities which were not those of the company issuing the challenged statements; b) Plaintiffs found just a handful of situations wherein unique factors allowed plaintiffs to meet the "in connection with" requirement when they purchased a security other than the company issuing statements;[11] and c) the district court cited only

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[11] *See Semerenko,* 223 F.3d at 175 (misrepresentations by Cendant about Cendant during a tender offer for shares of ABI stock "in connection with" plaintiffs' purchases of ABI stock); *Muzinich* No. CV-01-284-5BLW, slip op. at 9 (in expressly rejecting the standing argument accepted by the Second Circuit, Court held that plaintiffs' purchases of WGI shares were "in connection with" *Raytheon's* misrepresentations about the value of its subsidiary, which was later sold to WGI) (A-661); *Masnik v. Bolar Pharm. Co., Inc.,* No. 90-4086, 1991 WL 138331, #3-6 (E.D. Pa. July 18, 1991) (Misrepresentations by Bolar executives concerning Bolar's generic competitor to SmithKline's drug were in connection with plaintiffs' sales of SmithKline stock); *Crofoot v. Sperry Rand Corp.*, 408 F. Supp. 1154, 1156-58 (E.D.

several cases holding that plaintiffs who do not buy a security at all or do not buy the security at issue in their lawsuit do not have standing. *See, e.g., Inter-County Res., Inc. v. Med. Res., Inc.*, 49 F. Supp. 2d 682, 683 (S.D.N.Y. 1999) (Plaintiffs must be purchasers or sellers "of the securities *at issue in the claim* . . .") (emphasis added).[12]

The harm to investors and the integrity of the markets which likely will be inflicted by the Opinion far outweighs the hypothetical, wholly unsubstantiated, concern of vexatious litigation. Numerous other safeguards preclude the Second Circuit's policy concerns from coming to fruition. Initially, the fact-intensive "in connection with" requirement provides courts with ample power to dismiss cases where, unlike here, the nexus between investors' injuries and defendants' misrepresentations is unclear. *See, e.g., Semerenko*, 223 F.3d at 175 ("in connection with" requirement must be assessed on a case-by-case basis). While "in connection with" in an efficient market case is satisfied by a showing that defendants' statements were material and materiality is not typically an issue to be decided as a matter of law, courts have not hesitated to do so when plaintiff's pleading is devoid of allegations demonstrating its existence. Moreover, plaintiffs must allege and prove loss causation and must be able to satisfy the PSRLA's pleading requirements pertaining to defendants' scienter. Accordingly, there is no reason to interpret Section 10b and Rule 10b-5 as precluding standing simply because the defendant issuing the challenged statements was not also the issuer of the stock purchased by plaintiffs,

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Cal.1976) (statements by *Sperry Rand* regarding its computer system were "reasonably calculated to influence the investigating public," and were "in connection with" the plaintiffs' purchases of another company's stock since Sperry discussed the sale of its computers to that company). The Opinion would, of course, mandate the denial of standing in each of these cases, demonstrating, once again, the breadth of the Opinion's denial of relief to investors.

12 Here, Plaintiffs' claims pertain to the very security at issue in their claims. Thus, the only law cited by either the lower court or the Second Circuit confirms Plaintiffs' standing.

particularly given that doing so is directly at odds with the text of the statute and this Court's *Blue Chip* opinion.

CONCLUSION

For all the foregoing reasons, Petitioners respectfully request that the Supreme Court grant review of this matter.

Respectfully submitted,

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